IIMG
International Investment
Management Group

Market Commentary

May 2022

CONTINUED MARKET HEADWINDS AS BOND MARKETS TUMBLE

April was the month reality set in for investors that the myriad headwinds facing the global economy and financial markets are not about to alleviate any time soon and could magnify beyond current expectations.

Stock markets sold off sharply in a three-day rout in late April and ended the month deep in the red. The US S&P500 and Nasdaq led global equity markets downwards, with the former shedding 8.7% and the latter 13.3% in April alone. For the year, the Nasdaq has lost more than 21.1% and the S&P500 12.9%.

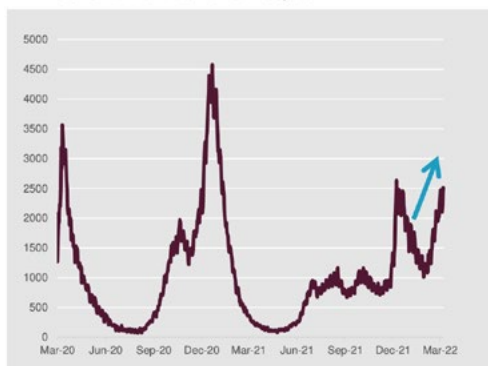
China was also hard hit, extending its losing run that was set in motion last year when the Chinese authorities clamped down on tech and online industries, imposing much harsher regulations on their business activities. This year the world's second largest economy has been dogged by ongoing Covid flareups, with Shanghai under strict lockdown during April and growing fears that Beijing may be next in line.

Elsewhere, Covid is proving less disruptive because even though numbers are rising, deaths are not and countries such as the UK are learning to live with the virus in the absence of a new more virulent strain emerging.

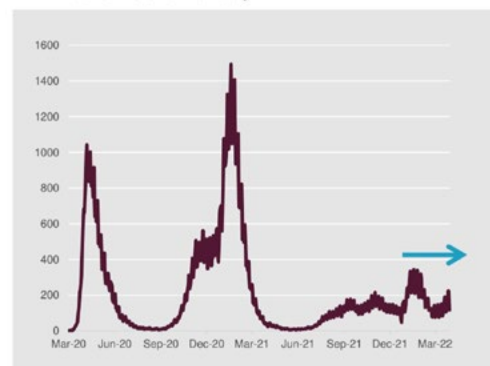
"HEADWINDS FACING THE GLOBAL ECONOMY AND FINANCIAL MARKETS ARE NOT ABOUT TO ALLEVIATE ANY TIME SOON"

Vaccine policy keeping Covid fears muted
Flare-ups less likely but disruptions remain a wild card. Example: UK

ADMISSIONS UK Covid-19 Hospital



DEATHS UK Covid-19 Daily



Source: FTSE Russell

Learning to live with inflation

Bond markets had their worst ever month, with yields jumping higher on concerns that the central banks may become overzealous in their implementation of more restrictive monetary policy conditions via higher interest rates and quantitative tightening. In both the US and Europe, indices of bonds with maturity greater than 10 years have declined in value by over 15% YTD.

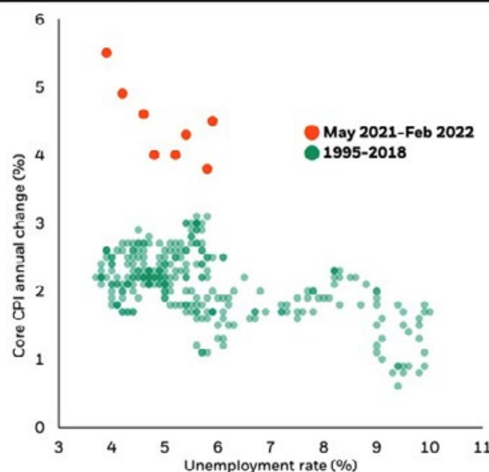
With inflation at forty-year highs, the US Federal Reserve is still on track to raise the federal funds rate by at least 50 basis points at its next meeting. Moving forward, there is a growing argument that the Fed will take into account the potential for monetary conditions to tighten for other reasons, and that inflation is close to peaking.

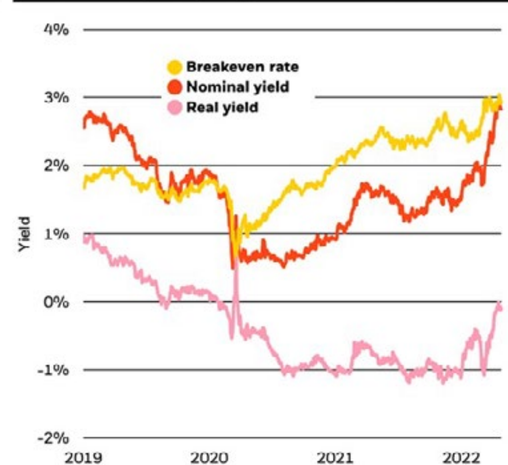
BlackRock and FTSE Russell see the central banks as learning to live with inflation. Notwithstanding projections of a series of rate hikes this year, they believe the central banks are likely to maintain low real yields, cognisant of the risks of reversing their quantitative easing policy too sharply. Excessive tightening could destroy demand and lead to a rise in unemployment.

Despite the hawkish tone, central banks will be wary of raising rates too quickly.

“BOND MARKETS HAD THEIR WORST EVER MONTH”

Global Outlook

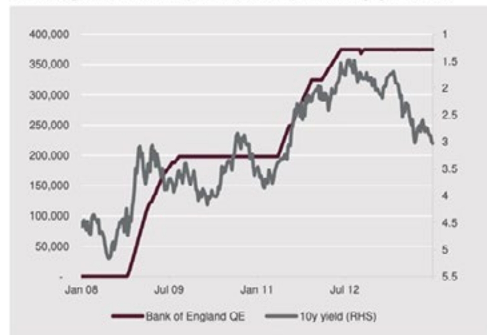




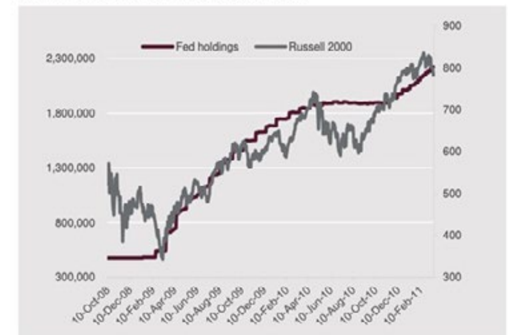
Source: Blackrock

QE affected risk assets and rates positively
Central banks are highly aware of the positive effects that QE has brought and equally aware of the risks of reversing the policy

10y gilt yields rallied during BofE QE, Holdings £millions (forward 6m) and 10y yield, %



Russell 2000 decisively rallied on the back of QE, $trillions of QE and Russell 2000



Source: FTSE Russell

“THE WORLD ECONOMY IS STILL EXPECTED TO AVOID RECESSION THIS YEAR”

Downgrading growth forecasts

The IMF, the World Trade Organisation and private sector economists are still factoring in a material slowdown in the global economy this year, downgrading their growth forecasts to reflect inflation, hawkish central banks, the ongoing Ukraine-Russia war and extended supply constraints, with China still set on maintaining its zero-Covid strategy.

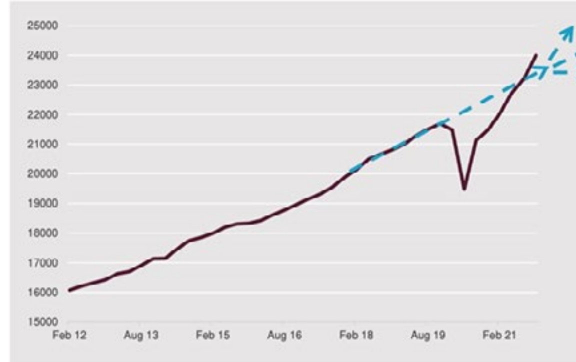
The IMF downgraded its economic growth forecasts across 143 countries that account for 86% of global GDP, with global economic growth now expected to come in at 3.6% in both 2022 and 2023 - 0.8 ppt and 0.2 ppt lower than the growth projected in January this year.

The WTO is even more pessimistic, expecting world GDP to increase by a mere 2.8% this year and to pick up to 3.2% next year. The Peterson Institute for International Economics (PIIE) predicts that global economic growth will come in at 3.3% in both 2022 and 2023.

Clearly, recession is still not a base-case scenario but Europe is perhaps the region most vulnerable to this downside scenario. Despite the sharp deterioration in investor sentiment of late and material downgrades in growth forecasts, the world economy is still expected to avoid recession this year.

GDP growth and forecasts look robust
Optimistic backdrop: Rate-hike expectations have been fuelled

US GDP



Robust everywhere, Consensus forecasts

Latest consensus GDP forecasts
%, January 2022

	2021	2022	2023
US	5.6	3.8	2.5
UK	7.2	4.5	2.2
Eurozone	5.2	4.0	2.4
Japan	1.6	3.0	1.3
China	8.1	5.2	5.2
Canada	4.7	3.8	3.1

Source: FTSE Russell

US elections loom on the horizon

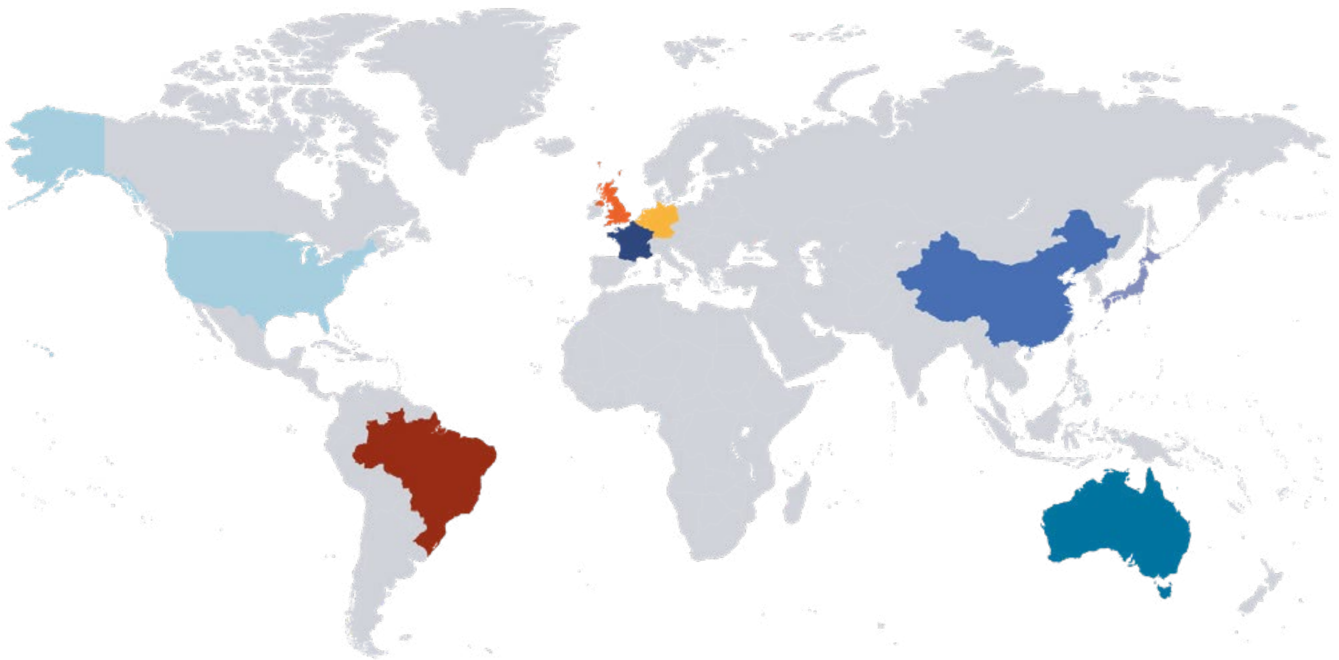
“THE PREVAILING VIEW IS THAT REPUBLICANS COULD WELL TAKE BACK BOTH CHAMBERS OF CONGRESS”

Ahead for the US are the mid-term elections in November, which will inevitably affect the mood of the electorate. The prevailing view is that Republicans could well take back both chambers of Congress, which could result in policy gridlock.

Although markets tend to take such outcomes in their stride, it may increase volatility as policy differences become more apparent.

Republicans taking control of the House and the Senate is likely to result in fewer tax changes, greater increases in defence spending, fewer green initiatives and some contentious negotiations around the debt ceiling. That compares with the status quo, namely a moderate increase in defence spending, further climate bills aimed at putting in place green incentives and an easier path to raising the debt limit. We will doubtless see greater focus on the implications as the time nears.

GLOBAL MARKET RETURNS - APRIL 2022



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